

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Date:

November 09, 2011

Legend

Company =

State =

Date1 =

Date 2 =

Date 3 =

Date4 =

Date5 =

Date6 =

Date7 =

Date8 =

Trust1 =

Trust2 =

A =

B =

C =

D =

Court =

Dear :

This letter responds to your letter dated June 3, 2011, and subsequent correspondence, submitted on behalf of Company, requesting a ruling under § 1362(f) of the Internal Revenue Code (Code).

Facts

Company was incorporated under the laws of State on Date1 and elected to be an S corporation effective Date2. On Date3 and Date4, A transferred shares of Company's stock to Trust1 for the benefit of A's spouse, B. On Date5 and Date6, C transferred shares of Company's stock to Trust2 for the benefit of C's spouse, D. It was intended that Trust1 and Trust2 be trusts that were treated under subpart E of part I of subchapter J of chapter 1 of the Code (grantor trusts) as owned entirely by A and C, respectively, and, thus, eligible shareholders under § 1361(c)(2)(A)(i).

On Date7, Company learned that the trusts were not eligible S corporation shareholders under § 1361(c)(2)(A)(i) because Trust1 and Trust2 were not grantor trusts owned entirely by A and C, respectively. Accordingly, Company's S corporation election had terminated on Date3 when A transferred shares of Company's stock to Trust1. After learning that Company's S corporation election had terminated, the trustees of Trust1 and Trust2 petitioned Court to reform the trusts so that Trust1 and Trust2 qualify as grantor trusts owned entirely by A and C, respectively. On Date8, Court granted the petitions to reform Trust1 and Trust2.

Company represents that there was no intent to terminate Company's S corporation election and that the transfer of Company's stock to Trust1 and Trust2 was inadvertent and not motivated by tax avoidance or retroactive tax planning. Company also represents that Company and its shareholders have treated Company as an S

corporation from Date3 and thereafter. In addition, Company and its shareholders have agreed to make any adjustments consistent with the treatment of Company as an S corporation as may be required by the Secretary with respect to the period specified by § 1362(f).

Law

Section 1361(a)(1) provides that the term “S corporation” means, with respect to any taxable year, a small business corporation for which an election under § 1362(a) is in effect for such year.

Section 1361(b)(1) defines the term “small business corporation” to be a domestic corporation which is not an ineligible corporation and which does not (A) have more than 100 shareholders, (B) have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than one class of stock.

Section 1361(c)(2)(A)(i) provides that, for purposes of § 1361(b)(1)(B), a trust all of which is treated (under subpart E of part I of subchapter J of chapter 1 of the Code) as owned by an individual who is a citizen or resident of the United States may be a shareholder of an S corporation.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the first day of the first taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation.

Section 1362(f) provides, in part, that if (1) an election under § 1362(a) by any corporation was terminated under § 1362(d)(2) or (3); (2) the Secretary determines that the circumstances resulting in such termination were inadvertent; (3) no later than a reasonable period of time after discovery of the circumstances resulting in such termination, steps were taken so that the corporation for which the termination occurred is a small business corporation; and (4) the corporation for which the termination occurred, and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), agrees to make the adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to this period, then, notwithstanding the circumstances resulting in the termination, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Conclusion

Based solely on the facts submitted and representations made, we conclude that Company's S corporation election was terminated on Date3 when Trust1 acquired Company's stock. We further conclude that the termination was inadvertent within the meaning of § 1362(f). In addition, to the extent Company's S corporation election would have terminated on Date4, when A transferred additional shares of Company's stock to Trust1, or on Date5 or Date6, when B transferred Company's stock to Trust2, such terminations were inadvertent within the meaning of § 1362(f). Pursuant to § 1362(f), Company will continue to be treated as an S corporation from Date3 and thereafter, unless Company's S corporation election is otherwise terminated under § 1362(d).

Except as expressly provided herein, we express or imply no opinion concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Under a power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

Sincerely,

Mary Beth Carchia
Senior Technician Reviewer, Branch 3
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2)

A copy of this letter
A copy for § 6110 purposes

cc: